No. 581

In the Supreme Court of the United States

October Term, 1944

Commissioner of Internal Revenue, petitioner

v.

Court Holding Company

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE PETITIONER

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OPINIONS BELOW

The opinion of the Tax Court (R. 86–102) is reported in 2 T. C. 531. The opinion of the Circuit Court of Appeals (R. 117–122) is reported in 143 F. 2d 823.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on July 11, 1944 (R. 123.) The petition for a writ of certiorari was filed on October 11, 1944, and was granted on November 20, 1944 (R. 124). The jurisdiction of this Court rests on Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the Tax Court committed reversible error in holding that a sale, formally made by the corporate taxpayer's two shareholders, was, in substance, a sale by the taxpayer, the gain from which was attributable to it.

STATUTE AND REGULATIONS INVOLVED

Internal Revenue Code:

> SEC. 22. GROSS INCOME.
>
> (a) *General definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * * (26 U. S. C. 22)

Treasury Regulations 103, promulgated under the Internal Revenue Code:

> SEC. 19.22 (a)–19. *Sale of capital assets by corporation.*—If property is acquired and later sold for an amount in excess of the cost or other basis, the gain on the sale is income. If, then, a corporation sells its capital assets in whole or in part, it shall include in its gross income for the year in

which the sale was made the gain from such sale, computed as provided in sections 111 to 113, inclusive. If the purchaser takes over all the assets and assumes the liabilities, the amount so assumed is part of the selling price.

* * * * *

SEC. 19.22 (a)–21. *Gross income of corporation in liquidation.*—When a corporation is dissolved, its affairs are usually wound up by a receiver or trustees in dissolution. The corporate existence is continued for the purpose of liquidating the assets and paying the debts, and such receiver or trustees stand in the stead of the corporation for such purposes. (See sections 274 and 298.) Any sales of property by them are to be treated as if made by the corporation for the purpose of ascertaining the gain or loss. No gain or loss is realized by a corporation from the mere distribution of its assets in kind in partial or complete liquidation, however they may have appreciated or depreciated in value since their acquisition. But see section 44 (d) and section 19.44–5. (See further section 19.52–2.)

STATEMENT

The facts as found by the Tax Court (R. 87–93) may be summarized as follows:

Taxpayer, a Florida corporation, was organized in 1934 to acquire title, at a foreclosure sale, to an apartment building in Miami Beach. This

was its only asset. Of its fifty shares outstanding, forty-eight were owned by Minnie Miller and the other two by her husband, Louis Miller. In 1938, taxpayer leased the building to Aaron and Regina Feiwish for three years commencing October 1, 1938. Some time after October 1, 1939, the Feiwishes, together with a sister and brother in-law of Mrs. Feiwish, the Fines, began negotiations with Minnie Miller for the purchase of taxpayer's property. In February, 1940, Louis Miller, acting as president of taxpayer, agreed to sell and the Fines agreed to purchase the property for $54,500. The terms of sale were agreed upon, and on February 22, 1940, the parties and their attorneys met for the purpose of having the oral agreement reduced to writing and executed. The attorney for the Fines prepared a contract embodying the terms of the oral agreement, but the writing was never executed by the corporation. Either at the meeting of February 22, or within the next two days, taxpayer's attorney advised the purchaser that taxpayer could not consummate the sale, for the reason that it would result in the imposition of a large income tax. (R. 87–89.)

On February 23, 1940, taxpayer's attorney and accountant met with Minnie and Louis Miller, and Harry Miller, their son (R. 84). The three Millers, constituting all of taxpayer's directors, then held a special meeting at which it was re-

solved that "it would be in the best interest of the corporation to have it declare a dividend payable in the assets of the corporation, in complete liquidation and surrender of all the outstanding corporate stock." Immediately thereafter, Louis and Minnie Miller, as stockholders, held a special meeting and adopted a resolution ratifying the action of the directors. On the same afternoon, subsequent to adoption of these resolutions, a deed conveying taxpayer's property to Louis and Minnie Miller jointly was executed on taxpayer's behalf by Louis Miller as president, and attested by Harry Miller as secretary. Thereafter, the attorney for the purchaser was notified of the change in title and was requested to prepare a new contract naming the Millers individually as vendors. The contract was drawn, providing for the same purchase price and embodying the same terms and conditions as had been previously agreed upon at the meeting of February 22, except for a correction in the amount stated to be the unpaid balance of an existing mortgage to which the sale was subject. It was executed by the Millers as vendors and by Margaret W. Fine as purchaser on February 26, 1940. The deed from taxpayer to the Millers was recorded the same day. (R. 89–90.)

The contract between the Millers and Mrs. Fine recited the receipt of a down payment of $1,000; this represented a credit against the purchase

price of a rent payment in that amount made by the Feiwishes to taxpayer on January 5, 1940. The balance of the purchase price, amounting to $53,500, was payable in the amount of $12,500 in cash upon closing, by the assumption of an existing first and second mortgage, and the execution of a purchase money note and third mortgage. Two thousand dollars which had been deposited with taxpayer by the Feiwishes as security for performance of the lease was applied in reduction of the purchase money note and third mortgage. Taxpayer has transacted no business nor owned any property since the liquidation distribution, but has not been formally dissolved. (R. 90–91.)

In its 1940 return, taxpayer reported no gain as having been realized from the sale. In her individual return for 1940, Minnie Miller reported a long-term capital gain on the exchange of her stock for taxpayer's assets, of which fifty percent was taken into account. The Commissioner determined that taxpayer realized a taxable gain on the sale and computed a deficiency accordingly (R. 91–93). The Tax Court affirmed his determination (R. 93–101). The Circuit Court of Appeals reversed, one judge dissenting (R. 117–122).

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred:

1. In substituting its view of the facts for those found by the Tax Court.

2. In holding that the Tax Court was required, as a matter of law, to find that the sale was made by taxpayer's stockholders.

3. In holding that any formally perfect liquidation distribution by a corporation must be recognized for tax purposes, even though the distribution has no reality or business substance and is admittedly resorted to solely for tax avoidance purposes.

4. In failing to apply to the facts of this case the established principle that the substance rather than the form of a transaction is determinative of its tax consequences.

5. In reversing the judgment of the Tax Court.

SUMMARY OF ARGUMENT

The Tax Court concluded that the real vendor was taxpayer corporation, not its two stockholders. In reversing, the court below rested its decision upon two inconsistent grounds: (1) Taxpayer "called off" its oral sale agreement and made a bona fide liquidation distribution to its stockholders; (2) taxpayer refused to bind itself in writing, and was therefore legally "free" to consummate the same oral agreement by passing title to its stockholders, in the form of a liquidation distribution, for the sole purpose of enabling the latter to substitute themselves individually as vendors. On either premise the court below erred.

To the extent that the decision below is predicated on the assumption that taxpayer abandoned

the oral agreement and made a genuine liquidation distribution, it violates the settled principle that it is the function of the Tax Court, not the Circuit Court of Appeals, to find the facts and draw inferences from them. The Tax Court made a directly contrary finding and the record unquestionably supports its determination. In substituting its own view of the facts for that of the Tax Court, the court below disregarded the limitations upon the scope of appellate review repeatedly expressed by this Court.

To the extent that the decision below rests on the theory that taxpayer was free to consummate the same oral agreement, for tax avoidance purposes, by routing title to the purchaser via a liquidation distribution to its stockholders, it violates the established principle, affirmed by this Court in a variety of contexts, that tax consequences flow from the substance of a transaction, not the form in which it is cast. The boundaries of tax avoidance do not encompass resort to legal mechanisms having no business object and designed solely to disguise a taxable event. In relieving corporations of tax liability upon a liquidation distribution of appreciated assets in kind, the applicable regulation is patently aimed at real liquidations; the relief was not intended to benefit a corporation which effects a "straw" liquidation distribution for the single avowed tax-avoidance purpose of having its stockholders act

as conduits of title to a purchaser already found upon terms of sale already agreed upon. The circuitous manner in which the sale was here consummated did not as a matter of law preclude the Tax Court from finding that the sale was in fact made by taxpayer. Whether the liquidation distribution was real or a sham is a question of fact within the province of the Tax Court to determine.

ARGUMENT

Section 22 (a) of the Internal Revenue Code, *supra*, p. 2, broadly defines gross income as including gains from sales of property. Section 19.22 (a)–19 of Treasury Regulations 103, *supra*, pp. 2–3, provides that "If, then, a corporation sells its capital assets in whole or in part, it shall include in its gross income for the year in which the sale was made the gain from such sale, computed as provided in sections 111 to 113, inclusive." Section 19.22 (a)–21 of the same regulations provides that "No gain or loss is realized by a corporation from the mere distribution of its assets in kind in partial or complete liquidation, however they may have appreciated or depreciated in value since their acquisition." [1]

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[1] Provisions corresponding to Sections 19.22 (a)–19 and 19.22 (a)–21 of Regulations 103 appeared in the regulations issued under the successive revenue acts since the 1918 Act; as Section 22 (a) to which they apply has remained substantially the same, they are deemed to have received Congressional approval. *Helvering* v. *Winmill*, 305 U. S. 79, 82–83.

The issue in this case was succinctly stated and resolved by the Tax Court as follows (R. 96):

> The facts then may be narrowed down to this: The petitioner having entered into an oral contract to sell its property, and having received payment of part of the agreed price, at the last moment, and admittedly for the sole purpose of avoiding taxes, distributed the property to its stockholders, who promptly thereupon bound themselves in writing to perform individually the act which they had theretofore agreed to perform as a corporation. Under such circumstances we think it must be said that the Millers were carrying out the agreement made by the corporation and not an agreement made by themselves individually.

In reversing the Tax Court, the Circuit Court of Appeals rested its decision upon a combination of two incompatible "controlling" factors (R. 119–120): (1) That taxpayer "called off" the oral agreement. On this assumption the stockholders entered into and consummated an independent agreement of their own, since a sale concededly occurred. (2) That taxpayer did not execute a legally "binding" written agreement and, accordingly, was "free" to declare that it would not "go forward with the sale" in its own name but could pass title to its stockholders, in the form of a liquidation distribution, for the sole purpose of enabling them to go forward upon the "same terms" in their own names. On this hypothesis,

of course, the oral agreement was not abandoned; the stockholders merely consummated individually the agreement they had negotiated on behalf of the corporation and all that was "called off" was the identity of the vendor.

On either premise, we submit, the court below erred in reversing the Tax Court's decision.

I

THE COURT BELOW DISREGARDED ESTABLISHED PRINCIPLES GOVERNING THE SCOPE OF APPELLATE REVIEW OF TAX COURT DECISIONS BY ASSUMING, CONTRARY TO THE TAX COURT'S FINDINGS, THAT TAXPAYER ABANDONED ITS ORAL AGREEMENT AND EFFECTED A BONA FIDE LIQUIDATION

Insofar as the decision below is premised on the inference that taxpayer abandoned the oral agreement and made a bona fide liquidation distribution, it violates the settled principle that it is the function of the Tax Court, not the Circuit Court of Appeals, to weigh the evidence, find the facts, and draw inferences from the facts. *Dobson* v. *Commissioner,* 320 U. S. 489, rehearing denied, 321 U. S. 231; *Wilmington Co.* v. *Helvering,* 316 U. S. 164, 168; *Commissioner* v. *Scottish American Investment Co.,* decided by this Court December 4, 1944, not yet reported.

In assuming that the oral agreement was "called off" (R. 120), the majority of the court below substituted its own view of the facts for that of

the Tax Court. For the Tax Court had concluded that the stockholders "were carrying out the agreement made by the corporation and not an agreement made by themselves individually"; that "it was always intended and understood by the parties that the sale would be made exactly as agreed by the petitioner, except for the change in identity of the vendor"; that "consummation of the oral agreement was the substantive purpose" of the ensuing liquidation distribution and substitution of the stockholders as nominal vendors (R. 96); that the stockholders acted as agents of the corporation in consummating the agreement; that "the contract which was executed and the sale which was consummated were in substance the petitioner's contract and sale" (R. 97); and that "the sale, although in form by the stockholders, was in reality in performance of the prior agreement" (R. 101).

In assuming that the corporation was "actually" liquidated (R. 120), the majority of the court below likewise substituted its own view of the facts for that of the Tax Court. For the Tax Court had concluded (R. 96–97) that the resolutions to liquidate and the liquidation distribution were not bona fide but "were formal devices to which resort was had only in the attempt to make the transaction appear to be other than what it was".

The statement of the majority of the court below (R. 120) that the corporation was "defunct"

and could not be "resurrected to be taxed for a sale it did not make" begs the point at issue, ignores the Tax Court's finding (R. 91) that taxpayer has not been formally dissolved, and is also at variance with its own previous observation (R. 119) that under Florida law the corporation remains "intact for a time to settle its affairs".[2]

And in reaching the ultimate conclusion that the sale was in fact and substance a sale by the stockholders individually, the majority of the court below replaced the inference drawn by the Tax Court with its own.

We submit that the correct view of the case was that stated in the dissenting opinion below (R. 122):

> The determination, therefore, whether a transaction of this kind was one of a real refusal of the corporation to sell, a real liquidation, re-negotiation with the purchaser by the stockholders, or was a sham refusal and a carrying out of the original plan through the stockholders as agents, presents a field for fact finding, a field in short in which the finding of the Tax Court is controlling.

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[2] Whether taxpayer was dissolved manifestly has no bearing on the question whether it was the real vendor. If, as the Tax Court found, taxpayer made the sale, it is liable for tax on the gain, and its stockholders, as transferees of its assets, could be compelled to discharge the unpaid corporate tax. *Phillips* v. *Commissioner*, 283 U. S. 589. See also infra, p. 28.

There can be no question here that there is a substantial basis in the evidence for the Tax Court's determination. The evidence shows that by February 22, 1940 all of the terms of a sale of taxpayer's property had been agreed upon with the purchaser, Margaret W. Fine, who was acting on behalf of the Feiwishes, the lessees of the property; that the parties and their representatives met that day at the office of the purchaser's attorney to execute a written contract embodying the oral agreement; and that taxpayer then refused to execute a written contract, giving as its reason that the sale would result in the imposition of a large income tax (Testimony of Schwartz, attorney for taxpayer (R. 26); Myers, attorney for the purchaser (R. 33); H. A. Miller (R. 26); L. Miller (R. 30); M. Miller (R. 85)). It also shows that taxpayer did not, however, forego the sale. On the following day, February 23, taxpayer's attorney and accountant met with its two stockholders, Louis and Minnie Miller, and their son Harry Miller; the three Millers held a special directors' meeting at which it was resolved to liquidate (R. 53–55) and at the conclusion of which Louis and Minnie Miller held a special stockholders' meeting to ratify this resolution (R. 55–57). On the same day a deed conveying taxpayer's property to Louis and Minnie Miller jointly was executed on taxpayer's behalf by Louis Miller as president (R. 58–60). The attorney for

the purchaser, who had meanwhile prepared the written contract naming taxpayer as vendor, was then notified of the change in title and requested to redraw the contract so as to substitute Louis and Minnie Miller individually as vendors; this he did on February 25 (R. 33). On the following day, February 26, the contract was executed by the Millers individually as vendors (R. 62–68), and the deed from taxpayer to the Millers was recorded the same day (R. 60). The contract recited the receipt by the Millers of a down payment of $1,000 (R. 62); this represented a credit against the purchase price of a previous rent payment by the Feiwishes to taxpayer (R. 85, 95–96). The sum of $2,000 which had been deposited by the Feiwishes with taxpayer as security under the lease was likewise applied against the purchase price by crediting that sum against the purchase money note and third mortgage given to the Millers (R. 70).

This evidence furnishes a solid foundation for the Tax Court's findings and for its conclusion that taxpayer did not abandon the oral agreement, but attempted rather to conceal its identity as the real vendor by resorting to a sham liquidation distribution. Indeed, the material facts are uncontroverted [3] and, as the dissenting opinion

[3] Taxpayer takes exception (Br. in Opposition, pp. 5–6) only to the finding (R. 90) that a $1,000 rent payment on January 5, 1940 was used as the $1,000 down payment against

below points out (R. 122), would appear to admit of no other inference. Without impugning the Tax Court's conclusion for lack of evidentiary support, the majority of the court below brushed it aside and bottomed its decision, in part at least, upon the contrary assumption that taxpayer "called off" the oral agreement and effected a bona fide liquidation distribution. In thus substituting its own view of the facts, the majority of the court below disregarded the repeated admonitions of this Court respecting the limitations on the scope of judicial review of Tax Court decisions, reiterated in *Dobson* v. *Commissioner, supra,* and again in *Commissioner* v. *Scottish American Investment Co., supra.*

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the purchase price which the sale contract recited (R. 62) as having been received by the Millers. This finding was fully explained by the Tax Court (R. 95–96), and taxpayer's motion for reconsideration of it was denied (R. 21–22). Moreover, it is clear from the Tax Court's opinion that this was but a cumulative factor entering into its determination, as was also the allied and undisputed finding (R. 91) that the \$2,000 deposited with taxpayer as security under the lease was applied in reduction of the purchase money mortgage. In any event, even assuming that the entire purchase price was received by the Millers individually, that would no more be determinative of the substance of the transaction than the fact that they had substituted themselves individually as vendors.

II

THE COURT BELOW ERRED IN HOLDING THAT THE TAX COURT WAS PRECLUDED BY THE FORM OF THE TRANSACTION FROM FINDING THAT THE SALE WAS IN FACT MADE BY TAXPAYER

Insofar as the decision below is predicated on the fact that taxpayer did not execute a binding written agreement in its own name, it violates the principle, affirmed by this Court in a variety of contexts, that tax consequences flow from the substance of a transaction, not the form in which it is cast. *Gregory* v. *Helvering*, 293 U. S. 465; *Minnesota Tea Co.* v. *Helvering*, 302 U. S. 609; *Griffiths* v. *Commissioner*, 308 U. S. 355; *Higgins* v. *Smith*, 308 U. S. 473; *United States* v. *Joliet & Chicago R. Co.*, 315 U. S. 44; *Lucas* v. *Earl*, 281 U. S. 111; *United States* v. *Phellis*, 257 U. S. 156. In applying the maxim that the reach of the income tax law is not to be delimited by refinements of title, this Court has uniformly held that income may be realized despite an anticipatory arrangement which prevents its passage into the taxpayer's hands. *Harrison* v. *Schaffner*, 312 U. S. 579; *Helvering* v. *Horst*, 311 U. S. 112; *Helvering* v. *Eubank*, 311 U. S. 122; *Helvering* v. *Clifford*, 309 U. S. 331; *Douglas* v. *Willcuts*, 296 U. S. 1; *Burnet* v. *Leininger*, 285 U. S. 136; *Old Colony Tr. Co.* v. *Commissioner*, 279 U. S. 716.

To hold, as did the court below, that a corporation which has orally agreed to sell its assets and has received part of the purchase price may escape tax liability on the gain resulting from the sale by conveying title to the purchaser via its controlling stockholders, exalts artifice above reality. And to consider the "controlling" fact to be that the corporation refrained from legally binding itself by a written agreement [4] sanctions, we believe, the kind of formalism which this Court has consistently refused to recognize as effectual to alter tax liability.

No valid reason exists for regarding the instant transaction as immune from operation of the doctrine enunciated in the above cases, and none was suggested in the opinion below. It is not enough to point out, as did the court below (R. 120), that a taxpayer may minimize taxes by any lawful means. The boundaries of tax avoidance do not encompass resort to legal mechanisms having no legitimate business object and designed solely to disguise the substance of the challenged tax event. The crucial question which remains, and to which the majority of the court below failed to address

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[4] The rationale of the decision below would apply with equal force in a situation where, after the corporation had executed a binding sale contract, it mutually agreed with the purchaser to rescind so as to render it "free" to make a liquidation distribution to its stockholders and substitute the stockholders as nominal vendors. The purchaser's agreement could be readily secured since acquisition of good title, not the identity of the vendor, is the purchaser's only concern.

itself, is whether the transaction under scrutiny is in fact what it appears to be in form.

The statute contemplates that if a corporation sells its property it is taxable on the resultant gain. Internal Revenue Code, Section 22 (a), *supra*, p. 2; Section 19.22 (a)–19 of Treasury Regulations 103, *supra*, pp. 2–3. On the other hand, a corporation may distribute its assets in kind, in complete or partial liquidation, without incurring tax liability, though the assets have appreciated in value since their acquisition. Section 19.22 (a)–21 of Treasury Regulations 103, *supra*, p. 3. In relieving the corporation of tax liability upon a distribution in liquidation of appreciated assets, the statute is patently aimed at a bona fide distribution; it was not intended to embrace a distribution which, though technically perfect and literally complying with the statute, is designed to cloak what is in reality a sale to a third party.

The record here unquestionably warrants the Tax Court's conclusion that what substantially occurred was a sale by taxpayer to a third party. For quite apart from taxpayer's admission that the sole purpose of the distribution in liquidation was tax avoidance, the conclusion is irresistible that the circuitous routing of the title to the purchaser via the stockholders was without reality or business substance. The corporate assets were not received by the stockholders to hold or use as their own, even temporarily, nor in proportion to

their stock holdings. The stockholders took title jointly, through a paper liquidation distribution, only to substitute themselves as vendors under the written contract embodying the self-same oral agreement they had negotiated and reached on behalf of their corporation. Amounts previously paid to the corporation as rent and as a security deposit under an outstanding lease of the property were credited against the purchase price, while the balance of the price was made payable to the stockholders. (R. 58–72, 88–91.) Not a single practical result was achieved by the stockholders' receiving transitory legal ownership and acting as conduit of the title which would not have been reached had the taxpayer simply and directly carried out its oral agreement, received the entire purchase price, and distributed the proceeds to its stockholders in liquidation.

In *Gregory* v. *Helvering*, 293 U. S. 465, the taxpayer's wholly owned corporation transferred securities to a new corporation, organized to avoid taxes, which issued all of its shares to the taxpayer, and which was subsequently dissolved and liquidated by the distribution of the securities to the taxpayer. It was held that although the transaction had the form of a corporate reorganization, it was without any business purpose and consequently the non-recognition provisions of the income tax law were inapplicable. This Court

examined the substance of the transaction and concluded that the newly organized corporation was nothing more than a contrivance (p. 469)—

> having no business or corporate purpose—a mere device which put on the form of a corporate reorganization as a disguise for concealing its real character, and the sole object and accomplishment of which was the consummation of a preconceived plan, not to reorganize a business or any part of a business, but to transfer a parcel of corporate shares to the petitioner.

To paraphrase the above language, the liquidation distribution here in question was a mere device which taxpayer sought to employ as a disguise for concealing a sale to a third party, and the sole object of which was the consummation of a preconceived plan not to distribute the assets to its stockholders but to transfer them to the purchaser.

The circumstance that the newly organized corporation in the *Gregory* case was not bound, in a formal legal sense, to distribute the securities to the taxpayer—the end sought to be achieved—did not prevent this Court from holding that the interposition of the new corporation was to be ignored. No more significant is the circumstance in this case that the taxpayer did not bind itself and its shareholders by executing a written contract.

The principle of the *Gregory* case was approved in *Minnesota Tea Co.* v. *Helvering*, 302 U. S. 609, 613–614. Both the reorganization provisions involved in the *Gregory* case and the liquidation-in-kind provisions here involved are aimed at relief from taxation. In both instances no gain or loss is recognized. In neither case, we submit, does a ritualistic compliance with the literal terms of the relief provisions suffice to give the taxpayer hoped-for advantages that were plainly intended for others. To grant the relief in this case would pervert the purpose of the liquidation-in-kind provisions in the same manner that the taxpayer unsuccessfully sought in the *Gregory* case to misuse the reorganization provisions.

In *Higgins* v. *Smith*, 308 U. S. 473, and *Griffiths* v. *Commissioner*, 308 U. S. 355, this Court refused to permit controlling stockholders to use the corporate entity to avoid individual taxes. Although this case presents, conversely, the tax liability of the controlled corporation, the broad principles underlying the decisions in those cases are applicable here. The attendant tax disadvantages of electing to do business as a corporation, which this Court, in the *Smith case* (p. 477), indicated must be accepted by the stockholders, include the tax burdens falling upon their controlled corporation. Cf. *Moline Properties* v. *Commissioner*, 319 U. S. 436; *Burnet* v. *Commonwealth Imp. Co.*, 287 U. S. 415.

In *United States* v. *Joliet & Chicago R. Co.*, 315 U. S. 44, this Court held that the umbilical cord

between a corporation and its stockholders is not severed merely because the corporation transfers its property under a contract which vests all rights thereunder directly in the stockholders; though the corporation has removed itself as conduit of the proceeds, the right of the stockholders remains derivative. This Court stated (p. 48):

> Payments made directly to shareholders by the lessee or transferee of corporate property are properly recognized as income to the corporation by reason of the relationship of a corporation to its shareholders. The fact that there is an anticipatory arrangement whereby the taxpayer is not even a conduit of the payments is no more significant in this type of case than it was in *Lucas* v. *Earl, supra.*

The anticipatory arrangement condemned in the *Joliet* case is little different, in substance and from the tax viewpoint, from that employed here. That taxpayer here invoked a "straw" distribution in liquidation as part of the arrangement can hardly suffice to insulate it from ownership of the purchase price which the purchaser paid directly to the stockholders. Cf. *Forest Glen Creamery Co.* v. *Commissioner,* 123 F. 2d 522 (C. C. A. 7th); *Sarther Grocery Co.* v. *Commissioner,* 63 F. 2d 68 (C. C. A. 7th).

In *General Utilities Co.* v. *Helvering,* 296 U. S. 200, the taxpayer corporation distributed shares of stock of another corporation as a dividend to its stockholders, who thereafter sold the shares to

a third party. The only issue litigated before the Board of Tax Appeals, on stipulated facts, was whether the shares were distributed as a dividend in kind or in satisfaction of a cash dividend. The Board concluded that it was the former and that therefore taxpayer realized no gain on the distribution. On appeal the Circuit Court of Appeals for the Fourth Circuit sustained the Board's determination of that issue, but proceeded to hold that the subsequent sale of the shares by the stockholders was in reality a sale by the corporation the gain from which was attributable to it (74 F. 2d 972). This Court reversed on the procedural ground that the question of the liability of the corporation as the real vendor had not been raised before or passed upon by the Board. Mr. Justice McReynolds, delivering the opinion of the Court, stated (pp. 206–207):

> Here the court undertook to decide a question not properly raised. Also it made an inference of fact directly in conflict with the stipulation of the parties and the findings, for which we think the record affords no support whatever. To remand the cause for further findings would be futile. The Board could not properly find anything which would assist the Commissioner's cause.

We are here confronted with no such procedural problem. In the *General Utilities* case the collateral question whether the corporation was

the real vendor was not litigated before the Board but the Circuit Court of Appeals attempted to determine it and, moreover, determined it "directly in conflict with the stipulation of the parties and the findings." Here, on the other hand, that question was the primary issue before the Tax Court, the Circuit Court of Appeals had the benefit of the Tax Court's findings on the issue, and the findings are unquestionably supported by the record. Whether or not in the *General Utilities* case the Circuit Court of Appeals' attempt to determine the issue *de novo* was warranted and whether or not a remand of the case to the Board would have been futile in the light of the facts there stipulated is of academic importance here, for the instant case presents the converse situation where the Circuit Court of Appeals has disregarded the Tax Court's conclusive determination of that factual issue. Cf. *Commissioner* v. *Scottish-American Investment Co., supra; Dobson* v. *Commissioner, supra.*

The lower federal courts have held consistently that where controlling stockholders of a corporation who have negotiated for the sale of corporate assets cause the corporation to transfer the assets to themselves (either by way of a "liquidation distribution" or a "sale"), and then consummate the sale individually, corporate tax liability is not foreclosed by the form of the transaction but the court will look to its substance

to determine whether the sale was in reality that of the corporation. *Meurer Steel Barrel Co.* v. *Commissioner,* 144 F. 2d 282 (C. C. A. 3d), petition for certiorari filed October 20, 1944 (No. 614); *Embry Realty Co.* v. *Glenn,* 116 F. 2d 682 (C. C. A. 6th); *S. A. MacQueen Co.* v. *Commissioner,* 67 F. 2d 857 (C. C. A. 3d); *Trafford Oil & Gas Co.* v. *Commissioner,* 78 F. 2d 814 (C. C. A. 3d), certiorari denied, 296 U. S. 630; *Liberty Service Corp.* v. *Commissioner,* 77 F. 2d 94 (C. C. A. 3d); *Nace Realty Co.* v. *Commissioner,* 28 B. T. A. 467, affirmed *per curiam* April 13, 1935 (C. C. A. 6th); *Boggs-Burnam & Co.* v. *Commissioner,* 26 B. T. A. 988, affirmed *per curiam* 71 F. 2d 999 (C. C. A. 6th). Cf. *Chisholm* v. *Commissioner,* 79 F. 2d 14 (C. C. A. 2d). Thus, in the recent case of *Meurer Steel Barrel Co.* v. *Commissioner, supra,* it was held that despite an elaborate liquidation plan whereby a corporation had transferred its assets to a partnership composed of some of its stockholders, a later sale by the partnership was in substance a sale by the corporation the gain from which was attributable to it. The Court distinguished the *Chisholm case, supra,* which also involved the transfer of corporate assets to a partnership that later sold them because the partnership there formed was a bona fide and continuing one, not a transitory device employed to escape tax. In *Embry Realty Co.* v. *Glenn, supra,* a corporation which had been

negotiating for the sale of some of its realty transferred the property in partial liquidation to its stockholders, who thereafter granted the prospective purchaser an option which culminated in a sale; it was held that though in form the transaction was a liquidation distribution and a sale by the stockholders, in substance it was a sale by the corporation. In *S. A. MacQueen Co.* v. *Commissioner, supra,* a corporation which made a sale to its president who later resold the property was held to be the real seller to the third party and taxable on the resultant gain.

It has also been uniformly held that where a corporation, in the course of liquidation, transfers its property to a trustee or agent for its stockholders, who thereafter sells the property, the sale is attributable to the corporation. *Hellebush* v. *Commissioner,* 65 F. 2d 902 (C. C. A. 6th); *Tazewell Electric Light & Power Co.* v. *Strother,* 84 F. 2d 327 (C. C. A. 4th); *Northwest Utilities Securities Corp.* v. *Helvering,* 67 F. 2d 619 (C. C. A. 8th), certiorari denied, 291 U. S. 684; *First Nat. Bank of Greeley, Colo.* v. *United States,* 86 F. 2d 938 (C. C. A. 10th); *Burnet* v. *Lexington Ice & Coal Co.,* 62 F. 2d 906 (C. C. A. 4th). See also *Steinberger* v. *United States,* 81 F. 2d 1008 (C. C. A. 9th). The same result is required by Section 19.22 (a)–21 of Treasury Regulations 103, which provides that sales made by trustees in dissolution "are to be treated as if made by

the corporation for the purpose of ascertaining the gain or loss". The Florida law, under which taxpayer was organized, provides that a corporation shall continue in existence for three years after dissolution for the purpose of paying its debts and winding up its affairs, and that its directors shall act as trustees in dissolution. Laws of Florida, 1925, c. 10096, Secs. 45–50; Florida Statutes (1941), Secs. 612.47–612.52. The corporate property is affected with a trust for the benefit of creditors, whose claims survive dissolution. *Howe* v. *Robinson*, 20 Fla. 352. The record does not disclose whether taxpayer had satisfied all debts before making the so-called liquidation distribution; but since taxpayer had the burden of proving the Commissioner's determination to be incorrect (*Welch* v. *Helvering*, 290 U. S. 111, 115), in the absence of proof to that effect we submit that its two stockholders must in any event be deemed to have acted as trustees in dissolution, not on their own behalf, in transferring the corporate assets to the purchaser and receiving part of the purchase price. This conclusion is also consonant with the familiar equity principle that dominant stockholders by virtue of their fiduciary relationship to the creditors of the corporation, may not deal with the corporate assets as their own. Cf. *Pepper* v. *Litton*, 308 U. S. 295, 306–307; *United States* v. *Joliet & Chicago R. Co.*, 315 U. S. 44, 48–49.

The reasons given by the court below for reversing the Tax Court's decision here appear to be wholly inconsistent with those upon which it relied in affirming that tribunal's decisions in *Commissioner* v. *Falcon Co.*, 127 F. 2d 277; *Trippett* v. *Commissioner,* 118 F. 2d 764, certiorari denied, 314 U. S. 644; and *Taylor Oil & Gas Co.* v. *Commissioner,* 47 F. 2d 108, certiorari denied, 283 U. S. 862. In the *Falcon* case, which also involved a post-liquidation sale by stockholders, it pointed out (p. 278) that the record disclosed "no * * * use of mere form to hide the substance of the real transaction", that the taxpayer corporation had "definitely decided not to sell", that "there was no sale contract in existence" when the property was distributed to the stockholders, that the liquidation distribution was "bona fide", that the stockholders thereafter entered into an "independent contract" of sale, and that the corporation received no benefit of any kind from the transaction. It accordingly held that "under the circumstance shown we agree with the Board" that the sale "was in truth and in fact" a sale by the stockholders. We submit that the very considerations which impelled the court below to sustain the Tax Court's determination in that case required affirmance of the Tax Court's opposite conclusion in this case. In the *Trippett* case, the court below, relying heavily upon *S. A. MacQueen Co.* v. *Commissioner, supra,* sustained the

Tax Court's determination that a sale by a corporation's two stockholders after a purported liquidation distribution of the property was attributable to the corporation; the rationale of its decision is that the stockholders could act only as agents in disposing of the corporate assets. And in the *Taylor* case, where a corporation, in order to avoid tax on a prospective sale, transferred the property to its directors as liquidating trustees, who thereafter made the sale, the court below sustained the Tax Court's determination that the gain was attributable to the corporation and aptly observed (p. 109) that "The real owner was still the company".

Whether a liquidation distribution is genuine, or merely a sham designed to conceal what is in reality a sale by the corporation to a third party, is essentially a question of fact in each case. That the question should be so regarded and dealt with has not hitherto been challenged. The decision below would remove a traditional field of fact-finding and inference-making from the province of the Tax Court by requiring it, as a matter of law, to give effect to the form rather than the substance of a transaction. It is broad enough to apply to both complete and partial liquidations, and affords a ready means of tax avoidance, particularly by family corporations. It is also an invitation to controlling stockholders who have reached an agreement to sell (or otherwise dis-

pose of) corporate assets to cause the corporation to make a last moment paper "liquidation distribution" of the property to themselves and to consummate the sale individually, for the single avowed purpose of escaping the corporate tax.

CONCLUSION

The judgment of the court below should be reversed.

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